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No. 06-231

IN THE

Supreme Court of the United States

CITIZENS FINANCIAL SERVICES, FSB (FORMERLY KNOWN AS CITIZENS FEDERAL SAVINGS AND LOAN ASSOCIATION), PETITIONER

v.

UNITED STATES

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

REPLY BRIEF

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REPLY BRIEF OF PETITIONER

Petitioner, Cititzens Financial Services, FSB ("Citizens"), respectfully submits this Reply in further support of its Petition for Writ of Certiorari, pursuant to Supreme Court Rule 15.6. This Reply is necessary because the government's Brief in Opposition ("Opp.") avoids the question presented in the Petition – the lower courts' application of a special rule requested by the government to limit the usual measure of lost profits damages to specific lost opportunities, an impossible and unjust standard on these facts, in conflict with nearly a century of jurisprudence from this Court, the Federal Circuit and other circuit courts of appeal. Citizens asks the Court to grant certiorari, vacate the judgment below and remand this matter for a proper consideration of long-established measures of damage.

1. In its Brief in Opposition, the government claims that because the Federal Circuit issued a judgment pursuant to Rule 36, "the order of the court of appeals does not adopt any rule of law, much less the purported 'special rule' that is the subject of the petition for certiorari." Opp. at 8. This Court, however, repeatedly has granted certiorari where the appellate court affirmed without opinion, even citing such affirmances as creating a conflict with a full opinion of another circuit. *See, e.g., Thomas Jefferson Univ. v. Shalala*, 512 U.S. 504, 511-12 (1994) ("The Third Circuit affirmed without opinion..., thereby creating a conflict with the decision of the Sixth Circuit"); *Mallard v. United States Dist. Court for Southern Dist. of Iowa*, 490 U.S. 296, 300 (1989) (granting certiorari and reversing where Eighth Circuit's order without opinion created conflict among circuits); *First Nat'l Bank of*

Logan v. Walker Bank & Trust Co., 385 U.S. 252, 253 (1966) (granting certiorari where Tenth Circuit's affirmance without opinion created conflict between circuits). Likewise, the Federal Circuit's decision without opinion in this case – implicitly finding, *inter alia*, no error of law under Fed. Cir. R. 36(e) and thus approving the reasoning of the trial court – has created conflicts between the Federal Circuit and (1) this Court; (2) other circuits; and (3) prior holdings of the Federal Circuit, itself.

Moreover, the government overlooks that this Court has frequently granted review of cases within the Federal Circuit's exclusive jurisdiction over contract claims against the government, recognizing that a conflict among the circuits may never arise, where the Federal Circuit has departed from the accepted course. Pet. at 23-24. Indeed, in *United States v. Winstar Corp.*, 518 U.S. 839 (1996), there was no conflict among the courts of appeals, yet this Court granted certiorari "to consider the extent to which special rules, not generally applicable to private contracts, govern enforcement of the governmental contracts at issue here." 518 U.S. at 860. In *Winstar*, this Court held that the government could not rely on such special rules to avoid *liability*. In *Mobil Oil Exploration & Producing Southeast, Inc. v. United States*, 530 U.S. 604 (2000), this Court, likewise granted certiorari without a conflict between circuits, and extended that principle to contract *damages*. *Id.* at 607, 614. Certiorari is similarly required here to clarify that special rules are not to be applied to a subset of damages, for lost profits.

2. The government next argues that "no question of general importance" is presented in this appeal. Opp. at 9. This argument again overlooks that

this Court has undertaken a special responsibility to review and intervene in the Federal Circuit's administration of cases within its exclusive jurisdiction, a matter of signal importance alone.

In addition, the issues raised in this appeal are not *Winstar*-specific, but involve fundamental questions of damage calculation and government contracting, above and beyond the universe of *Winstar* cases. Any argument by the government that this Court should not grant certiorari because this case is one of a diminishing number of *Winstar* cases, *id.*, is an affront to this Court's rulings in *Winstar* and *Mobil Oil* disavowing special rules that free the government of accountability from the law of contracts. More basically, it disregards the rationale behind this Court's holdings: that applying ordinary contract rules to government "ensures that [it] is able to obtain needed goods and services from parties who might otherwise, quite rightly, be unwilling to undertake the risk of government contracting."). *Winstar*, 518 U.S. at 883; *id.* at 913 (Breyer, J., concurring). Thus the government's argument of expediency, that any Federal Circuit acquiescence of special rules in *Winstar* lost profits cases is three-quarters complete, is no answer to the issue of general importance presented here of whether the Federal Circuit is enforcing traditional contract remedies needed to ensure that the government, for the benefit of itself as well as contractors, is viewed as a "reliable contracting partner." *Id.* at 883.

3. As for the merits, the government simply avoids the question presented in the Petition. As noted therein, the only way to escape the conclusion that Citizens could and did show lost profits in this case is to avoid the usual analysis entirely, as the courts did below in adopting a special rule limiting recovery to

specific lost opportunities. Having pressed this special rule at trial and before the Federal Circuit, the government disowns its former insistence upon a showing of specific lost opportunities, claiming now that "this case does not present any disagreement about the method of calculating damages in *Winstar* cases." Opp. at 10. Tellingly, the government's Opposition does not cite a single real instance where the courts below applied any other measure of lost profits.[1] In truth, the government had insistently framed the legal standard to require a showing of specific lost opportunities, inviting the error below.[2]

What actually are not in disagreement are the facts relevant to the usual measures of lost profits not allowed below. The government concedes that pre-FIRREA, Citizens was "a 'well-run shop with good capital, conservative . . . Low risk . . . well managed,'" Opp. at 3. The government does not dispute that in 1989, FIRREA immediately eliminated $30.5 million in supervisory capital, more than 50% of Citizens' $57 million in total capital, and phased-out another $8

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[1] The government falsely suggests that "the trial court expressly considered Citizens' pre-breach and post-breach history," Opp. at 12, n.5. The court only considered those facts in rejecting higher $20.9 million growth analysis under its alternative damages model, discussed *infra*. The court never considered those facts with respect to Citizens' $10.3 million pre-breach, post-breach or peer performance analysis.

[2] *See, e.g.*, Brief for Defendant-Appellee the United States at 25, *Citizens Fin'l Servs., FSB v. United States*, No. 05-5116 (Fed. Cir. filed Sept. 29, 2005)("To establish causation in fact of lost profits, a plaintiff must prove both that it would have made specific additional investments, funded by specific liabilities and that those additional investments would have been profitable in the but-for world.")

million through 1994, or 70% of its capital overall, Pet. at 5-6, that the government itself deemed Citizens' remaining capital "marginal," Pet. at 7 (citations omitted), and that the impact on Citizens was massive, or much like this Court has phrased the effects of FIRREA, "swift and severe." *Winstar*, 518 U.S. at 587.

The government further does not contest that Citizens was a traditional thrift that consistently earned profits on its assets both before and after FIRREA, with its average pre-tax returns on assets above 1.1%, comparable to the peer group developed by the government's expert, that pre-FIRREA Citizens grew its tangible assets 5% in 1987, and 5.3% in 1988 and had business plans anticipating continued growth by at least that same 5% rate in the next three years, that as a result of FIRREA Citizens reversed course and adopted a "no growth" strategy that it followed through mid-1993, after which it began to grow again. Pet. at 6-7 (citations omitted).

The government also does not dispute that following the breach in 1989, Citizens barely grew by a nominal .25% for four years through mid-1993, but during the same post-breach period, its local competitors grew their deposits at a compound annual rate of 7.64% according to Citizens' evidence (or 5% according to the government's own expert's peer group analysis). Pet. at 7 (citations omitted).

Upon such evidence, Citizens should have been allowed to prove and recover lost profits under ***any*** of the following standards: (1) a "before and after" comparison, based on its pre- and post-breach or injury performance, *see, e.g., Palmer v. Connecticut Railway & Lightning Co.*, 311 U.S. 544 (1941); *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251 (1946); *Eastman Kodak Co. v. Southern Photo Co.*, 273 U.S. 359, 376-78

(1927); *Sinclair Refining Co. v. Jenkins Petroleum Process Co.*, 289 U.S. 689, 697-98 (1933); ***or*** (2) a "yardstick" comparison to peers or industry averages, *see, e.g., Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 116 n.11, 123-25 (1927); *Bigelow, supra*; *Southern Pines Chrysler-Plymouth, Inc. v. Chrysler Corp.*, 826 F.2d 1360, 1364 (4th Cir. 1987); ***or*** (3) the loss of specific business or customers. While this third category of "loss of *specific* opportunities" is a permissible standard, it is not the exclusive method as the government insisted below, and now would concede.

As the government now also apparently concedes, other circuit courts have routinely calculated and awarded damages based on past or peer performance where the plaintiff was engaged in a high-volume business, like Citizens, without requiring proof of specific lost opportunities or particular lost sales. *See, e.g., Pitchford v. PEPI, Inc.*, 531 F.2d 92, 105, 108 (3d Cir. 1975) (noting it would be "unduly harsh" to require plaintiff to "document each sale that it might have made" because "the extent of such hypothetical sales was necessarily an estimate"); *see also, Lundell Mfg. Co. v. ABC, Inc.*, 98 F.3d 351, 35 (8th Cir. 1996) (plaintiff need not "identify specific lost sales to recover lost profits"); *In re M/V Nicole Trahan*, 10 F.3d 1190, 1195 (5th Cir. 1994) (proof of active market sufficient to entitle plaintiff to lost profits); *Bob Willow Motors, Inc. v. General Motors Corp.*, 872 F.2d 788, 798 (7th Cir. 1989) ("completely reasonable" to consider national sales trends to establish and calculate lost profits; plaintiff not required to identify specific or particular purchasers).

Thus, Citizens was entitled to prove its lost profits by its pre-breach performance, or post-breach performance, or peer or industry performance,

particularly where engaged in a high-volume business, as the government now states it is not in disagreement. Citizens, as a successful, conservative thrift prevented from expanding its existing business of making single family mortgages and buying mortgage-related securities, was not required to prove "specific investment opportunities" to establish lost profits. Instead, under controlling precedent, Citizens was entitled to and did show, at a minimum, that but for the breach it would have had a growth rate consistent with its pre-breach performance and plans and actual peer growth of 5% until 1993, and thereafter growth at its actual, faster rate, resulting in lost profits of $10.3 million based on its historical 1.1% return on assets.[3]

Yet the decisions below required Citizens to show "specific" investments that it was forced to forego, an artificial and arbitrary sole legal standard, *irrelevant to these facts*, instead of permitting Citizens to prove its lost profits by other bases long universally recognized, whether by pre-breach, post-breach, or peer performance.

The trial court's failure, with the Federal Circuit's acquiescence, to consider a proper claim for lost profits damages, not only disregards settled damages law, and conflicts with decisions of this and other courts, but violates this Court's admonitions that the "injured party is not to be barred from a fair recovery by impossible requirements." *Palmer*, 311 U.S. at 560-61. No less than in other cases that have come before this Court, "it would be a perversion of fundamental principles of justice to deny all relief to the

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[3] *See* J.A., *Citizens Fin'l Servs., FSB v. United States*, No. 05-5116 (Fed. Cir. filed Nov. 7, 2005), at A100037-38, A102394-98, A1004129-31, A104112-13, A400041-46, A400062-65, 82-84.

injured person, and thereby relieve the wrongdoer from making any amend for his acts." *Story Parchment Co. v. Paterson Parchment Paper Co.*, 282 U.S. 555, 563 (1931). And no matter who the wrong-doer may be, "the adoption of any arbitrary rule in such a case, which will relieve the wrong-doer from any part of the damages, and throw the loss upon the injured party, would be little less than legalized robbery." *Id.* at 565.

Had the courts below properly followed the precedents of this Court and the other circuits, and not erected an impossible barrier by special rule protective of the government, they would have been compelled to find that Citizens is entitled to damages of at least $10.3 million or, at the absolute minimum, a "jury verdict" award from the Court of Federal Claims pursuant to *Bluebonnet Savs. Bank, FSB v. United States*, 266 F.3d 1348, 1357 (Fed. Cir. 2001) (utilized "if there [is] clear proof of injury and there was no more reliable method for computing damages – but only where the evidence adduced was sufficient to enable a court or jury to make a fair and reasonable approximation").

The government's final arguments are straw men. The government seeks to avoid the inescapable conclusion that Citizens was entitled to prove lost profits through pre-breach performance, or post-breach performance, or peer or industry performance, by mischaracterizing Citizens' 10% capital goal. That goal, however, applied only to Citizens' alternative damages model, not to these ordinary measures of lost profits.[4]

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[4] Citizens' alternative damages model proceeded on the basis that, absent the breach, it would have grown to the extent permitted by its pre-breach 10% capital ratio and goal, amounting to lost profits of $20.9 million. Citizens' expert used that goal as a leverage ratio in order to estimate *how much* growth it would have obtained absent the breach that *only* applied to its $20.9 million growth

The government is similarly wrong in suggesting that Citizens passed up opportunities for growth in order to raise its capital cushion above the minimum required levels, as its regulators expected, and Citizens was entitled to maintain.[5]

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analysis; it was never suggested that the 10% capital ratio goal determined *whether* the breach forced Citizens to shrink, forgo growth and suffer lost profits. *See, e.g., LaSalle Talman Bank, FSB v. United States*, 317 F.3d 1363, 1371 (Fed. Cir. 2003) (discussing leveraging concept where non-breach asset growth derived by multiplying breached goodwill by capital ratio objective). At trial, Citizens attempted without success to prove that it would have grown faster than its prior 5% rate by using its "excess capital" over its pre-breach 10% level to support larger growth. The 10% leverage ratio was the input only in its higher damages model to estimate the amount of additional assets that could be supported at that level. The trial court, however, made no findings that Citizens would not have grown by at least its pre-breach modest growth rate of 5% or as fast as its peers.

[5] Citizens' capital ratio was 10.03% at the time of the breach. Post-breach, its capital was "marginal," as the government's regulators found and the government's expert admitted. The courts have recognized the right of banks to maintain a "capital cushion" for business reasons, and that such a decision did not negate causation. *See, e.g., Home Sav. of America, FSB v. United States*, 399 F.3d 1341, 1353 (Fed. Cir. 2005); *Long Island Sav. Bank, FSB v. United States*, 67 Fed. Cl. 616, 642 & n.21 (2005) ("Before the breach, the board operated the banks at a capital cushion near 8% for business reasons, and the board desired to operate Long Island [post-breach] at the same level."), *appeal dismissed*, 180 Fed. Appx. 930 (Fed. Cir. 2006); *Commercial Fed. Bank, FSB v. United States*, 59 Fed. Cl. 338, 347-48 (2004) *aff'd w.o. opn.*, 125 Fed. Appx. 1013 (Fed. Cir. 2005). Here, Citizens' post-breach capital ratios were comparable to national averages, particularly mutual thrifts and the local peer group identified by the government's expert. In fact, Citizens' capital ratios were below the government's expert's peer group during 1990-1992 and only slightly above them during 1993-1996. *See* J.A. *Citizens Fin'l Servs., FSB v. United States*,

For all these reasons, and as set forth in Citizens' Petition, certiorari is both appropriate and necessary to resolve the conflicts created by the error below, to ensure the Federal Circuit is not abdicating its role of enforcing the government's responsibility for its breaches of *Winstar* and other contracts, and to overturn an impossible barrier and special rule relieving the government of its financial obligations in a case where damages, arising from a devastating 70% loss of capital, were obvious.

CONCLUSION

The petition for a writ of certiorari should be granted.

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No. 05-5116 (Fed. Cir. filed Nov. 7, 2005), at A202007; A202026-28; A202030; A300022; A102246-47, 4022, 4027-4037; A103530-31, 4020.